PHILIP MORRIS MANAGEMENT CORP. INTER-OFFICE CORRESPONDENCE

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TO: Murray H. Bring DATE: June 25, 1996

FROM: Denise F. Keane

SUBJECT: *PM USA Legal Department Monthly Report - June 1996*

Herein follows a partial list of matters which our lawyers have been working on in June. Please let me know if you would like further details.

Corporate Affairs

In addition to the usual review and counseling, we reviewed media releases, speeches and publications and prepared contracts for The Accommodation Program in connection with its presence in Atlanta during the 1996 Summer Olympics. We also provided advice regarding the smoking lounges in the Atlanta airport.

Information Services

We continued to devote significant time to protecting the legal interests of PM USA in connection with the bankruptcy filing of Nelco Ltd. As previously reported, the bankruptcy court has approved a transaction in which Nelco will sell certain of its "lease pipeline" transactions to GE Capital Computer Leasing Corp. We are negotiating with GE the terms and conditions under which we would elect to complete our pipeline transactions with them.

We provided advice regarding an attempt by Computer Associates to extract significant additional license fees from us as a result of our proposal to move to a sysplex environment. The software licenses at issue are specific to a designated processor. The sysplex technology allows processors and databases to be linked, and Computer Associates claims that this entitles them to additional fees. Our position is that we will not be using sysplex to run application software across processors, and therefore, no additional fees are required.

We provided legal support for projects related to an upgrade of field sales equipment, the maintenance of the Integrated Retail Demographic database, the purchasing and accounts payable integration effort, Year 2000 system modifications, a master agreement with MSA, mobile disaster recovery services and video conferencing equipment and services.

We provided support in connection with the IS security initiative, including commenting on preliminary drafts of Baseline Standards for Information Security, an Internet Policy and a Client/Server policy.

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Marketing

In light of continuing construction delays and concerns with respect to the financial fortitud of Rader Railcar, the train manufacturer, we conducted a planning session with representatives of Hunton & Williams (national litigation and bankruptcy), Holland & Hart (local litigation and bankruptcy) and Hopkins & Sutter (special train counsel). We developed an action plan for responding expeditiously if and when our relationship with the manufacturer deteriorates. Centra to our discussion were plans for the lifting of a stay in bankruptcy and rights of replevin with respect to the recovery of Philip Morris property. We subsequently amended the construction agreement to obligate Rader Railcar to assist Philip Morris in efforts to perfect security interest and acknowledge prior transfers of title.

We began negotiating an agreement with Marketing Equities International to serve as the replacement for Rader Lightning Services and to provide Hotel Operations Services on board the Marlboro Unlimited train.

We began negotiating agreements with third parties retained in connection with ancillary events along the Marlboro Unlimited route for the payment of costs incurred in connection with 1996 trips postponed until 1997.

We continued to meet regularly with representatives of Rader Railcar, Bravo & Associates (Philip Morris' manufacturing expert), representatives of Richmond engineering and New York marketing to review and discuss open issues related to the engineering, construction and timeline for delivery of the Marlboro Unlimited train.

We assisted in the formulation and implementation of communications with the Marlboro Unlimited Sweepstakes potential winners.

Operations

We advised on the following agreements: Frigoscandia, Hyatt, Hoechst Celanese, Freight Revenue Recovery, Tranzact, Dixie Warehouse & Cartage, Jacobs-Sirrine Design Architectural Services and Union Camp.

We conducted a series of seminars for salaried employees at Park 500 and the BL Plant employees on business ethics and legal issues.

We continued to assist the Litigation group on local issues relating to document collection review and other matters.

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R&D

We continued to assist the Litigation group with local issues relating to various litigations including Castano, Humphrey and Tijerina, and with coordinating the document collection. We participated in meetings with R&D and Operations personnel to discuss witness preparation for various cases. We provided information to Australian counsel for the Cremona litigation.

We reviewed the Philip Morris patent portfolios on Delta and Sigma and identified two patents and possibly a third that may provide a position on Eclipse. We met with outside counsel to initiate validity and infringement studies.

A U.S. Patent was granted covering improvements relating to the humid-air reordering aspect of NET.

Sales

We participated in a strategy session with Sales senior management to discuss upcoming negotiations with Wal-Mart and McLane addressing our Retail Masters and private label agreements with these customers.

We prepared and/or reviewed contracts for the Trade Relations department for upcoming events including AWMA's summer convention, July Section Sales Director meeting and PM's C-Store Top-to-Top meeting in September. We also reviewed documents generated by the Genesis group addressing vendor managed replenishment and electronic data interchange with public warehouses and direct accounts.

We reviewed several software applications that will be rolled out to Field Sales Force management this year. The applications included Promotion Sell-In which "matches" demographic information about shoppers living within a store's market area with profile information about smokers of particular brands of cigarettes. We also reviewed Allocation Decision Support II, a software program that prioritizes workload accounts within a geographical area according to the objectives of a specific promotion.

We worked on an agreement pursuant to which 7-Eleven will handle the installation of PM fixtures at its Oklahoma stores.

We worked on a third-party warehousing agreement for POS and fixtures. This third-party facility will replace our present warehouse in New Jersey.

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Insurance/Vendor Action

In the Cappelli matters, we continued to work with outside counsel in eliciting and responding to settlement offers from defendants in the vendor actions. We worked on finalizing a settlement with Southern Container Corporation, a vendor defendant, and continued negotiations with C.D. Baird Company.

National Union Fire Insurance Company (AIG) recently moved to intervene in the Heinrich case, one of the federal court vendor actions. National Union is the excess insurer on PM's crime insurance claim. National Union refused to accept coverage of that claim, and now is a defendant in the insurance action pending in New York state court. National Union's asserted reason for the motion is to protect its "anticipatory and contingent subrogation claims." Having refused to pay the claim, we believe this claim is disingenuous. The real issue is that National Union objects to PM settling with Southern Container Company, without preserving National Union's "subrogation" rights. Under that settlement, Southern would pay PM a total of $6.5 million. National Union's motion included as annexures voluminous documents, including confidential documents PM provided to National Union (e.g., the Preliminary Proof of Loss Statement). We objected to National Union in writing. We are also exploring whether National Union's actions give rise to additional claims against it, e.g., bad faith claims, harassment or breach of fiduciary duty.

In addition, Federal Insurance Companies has moved to implead the vendors in the insurance action pending against Federal, the Chubb Group of Insurance Companies and National Union.

Miscellaneous

All of our lawyers participated in a PM USA management meeting in Chantilly, Virginia. We also participated in a panel presentation on legal/regulatory/external issues.

We have been contacted by the CPSC and have been asked to meet with them to discuss the Scripto Aim N Flame Lighters currently being offered as an on-pack incentive with Basic cigarettes. We have since learned that the CPSC received a petition (unrelated to our promotion) which challenges the utility lighter exemption which excludes ".....lighting device intended primarily for igniting materials other than smoking materials" from the regulations which impose a safety standard for disposal and novelty lighters. We will meet with the CPSC on June 26th.

We met with the Superslims litigation team to review trial preparations, discuss strategy, and assign pre-trial responsibilities to various team members.

We participated on an OAAA panel to discuss our Federal Legislative proposal and First Amendment issues.

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